UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF NEW YORK

In re:

CASE NO. 93-22321

David William Russell,

Debtor.

Joel R. Conklin,

Plaintiff,

vs. **A.P. NO. 95-2392**

David William Russell,

DECISION & ORDER

Defendant.

BACKGROUND

On October 21, 1993, the Debtor, David William Russell (the "Debtor"), who indicated that he was in the wholesale and retail florist business, filed a petition initiating a Chapter 11 case. On his Schedules, filed as required by Section 521 and Rule 1007, the Debtor listed: (1) as his only assets, miscellaneous personal property valued at $5,350.00, which did not include any checking, savings, brokerage or other financial accounts; and (2) unsecured obligations which totaled $195,562.67, including the amounts due on two judgments (collectively the "Conklin Judgment") obtained by Joel R. Conklin ("Conklin"), scheduled in the amount of $39,264.02, and a judgment (the "Edgar Judgment") obtained by Austin Edgar, Inc. ("Edgar"), scheduled in the amount of $19,661.86.

On January 27, 1994, the U.S. Trustee filed a Motion to Convert or Dismiss the Debtor's Chapter 11 case, and on March 1, 1997 an Order of Conversion was entered.

On January 27, 1994, the same day that the U.S. Trustee filed her Motion to Convert or Dismiss, Conklin commenced an adversary proceeding (the "Conklin Adversary Proceeding") which requested that the amounts due on the Conklin Judgment be determined by the Court to be nondischargeable pursuant to Sections 523(a)(2)(A), (a)(4), (a)(6) and (a)(7). The Complaint in the Conklin Adversary Proceeding alleged that the Conklin Judgment was based upon a number of separate causes of action to recover damages, including those resulting from: (1) the Debtor's alleged fraud in connection with Conklin's purchase of 10,000 shares of common stock in the Village Green Bookstores, Inc. (the "Village Green"); (2) the Debtor's failure to perform his obligations under a sub-lease of a 1988 Porsche (the "Porsche") which had been leased by Conklin from Porsche Financial Services ("Porsche Financial"); and (3) the Debtor's failure to pay a number of parking tickets which he received while using the Porsche which had remained registered to Conklin, and which Conklin was required to pay in order to be able to renew his New York State driver's license.

On June 8, 1994, an Order was entered discharging the Debtor from all of his debts with the exception of those which were the subject of the then pending Conklin Adversary Proceeding.

On March 8, 1995, after a trial in the Conklin Adversary Proceeding, the Court determined portions of the Conklin Judgment to be nondischargeable under Sections 523(a)(2)(A) and (a)(6).

On June 2, 1995, based on information discovered in the prosecution of the Conklin Adversary Proceeding, Conklin filed an Adversary Proceeding (the "Conklin Discharge Proceeding") which requested that the Debtor’s discharge be revoked by the Court pursuant to Sections 727(d)(1) and (d)(2).

The Complaint in the Conklin Discharge Proceeding included allegations that: (1) the Debtor had for a number of years hidden assets in his wife, Susan C. Russell's ("Susan Russell") name and used bank accounts in her name to run his businesses; (2) in his bankruptcy, the Debtor had failed to disclose a number of assets, including: (a) a brokerage account with Charles Schwab, Inc., maintained in joint names with his wife, opened in 1986 and closed in June, 1994; (b) a Dean Witter brokerage account (the "Dean Witter Account") maintained in the Debtor's name, opened in June, 1993; (c) a brokerage account maintained in Susan Russell's name, which was funded in whole or in part with funds from the Debtor's businesses; and (d) a bank account in the name of Selected Flowers (the "Selected Flowers Account") (3) prior to and while his Chapter 7 case was pending, the Debtor had negotiated checks in the names of various corporations in which he had an interest, and ran them through bank accounts maintained in Susan Russell's name; (4) before the filing of his Chapter 11 petition, while operating as a debtor-in-possession, and after the conversion of his case to a Chapter 7 case, all without disclosure to the Bankruptcy Court, the U.S. Trustee, his Chapter 7 Trustee or his creditors, the Debtor had continued to use Susan Russell's bank accounts to hide his business income; and (5) the Debtor's use of his wife's bank accounts and placing of assets in her name, both prior to his petition, during his Chapter 11 case, and after the conversion of his case to a Chapter 7 case, demonstrated a comprehensive and persistent pattern of fraud on creditors and the Bankruptcy Court.

On January 6, 1996, Edgar filed an Adversary Proceeding (the "Edgar Discharge Proceeding") which also requested that the Debtor's discharge be revoked by the Court pursuant to Sections 727(d)(1) and (d)(2). The Complaint in the Edgar Discharge Proceeding set forth

essentially the same allegations as contained in the Complaint in the Conklin Discharge Proceeding.

After the Debtor elected to proceed pro se in the Conklin and Edgar Discharge Proceedings, a joint trial was conducted on October 17 and 18 and November 18, 1996.

By a September 30, 1997 Decision & Order (the "Decision"), the Court, pursuant to Sections 727(d)(1) and (d)(2), revoked and denied the Debtor's discharge finding that Conklin and Edgar had proved by a preponderance of the evidence presented and admitted at trial that: (1) the Debtor's discharge was obtained through his fraud, and neither Conklin nor Edgar knew of such fraud until after his discharge was entered, in that the Debtor: (a) with intent to hinder, delay and defraud his creditors, the U.S. Trustee, the Court and his Chapter 7 Trustee, concealed property of the estate after the date of the filing of his petition; (b) without justification concealed financial records from which his financial condition or business transactions might be more fully ascertained; and (c) knowingly and fraudulently made false oaths or accounts; and (2) the Debtor had acquired property after the filing of his petition that was property of the estate, and he knowingly and fraudulently failed to report the acquisition of such property to the U.S. Trustee, the Court or his Chapter 7 Trustee, and neither Conklin nor Edgar discovered the existence of such property or the failure to report it until after the Debtor's discharge was entered.[1]

[1] The Decision is currently on appeal to the United States District Court for the Western District of New York (the "District Court").

On December 22, 1997, Conklin filed a motion (the "Sanction Motion") pursuant to Rule 9011 of the Rules of Bankruptcy Procedure[2] and related case law, which requested that the Court

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[2] Rule 9011 provides:

> (a) Signature. Every petition, pleading, motion and other paper served or filed in a case under the Code on behalf of a party represented by an attorney, except a list, schedule, or statement, or amendments thereto, shall be signed by at least one attorney of record in the attorney's individual name, whose office address and telephone number shall be stated. A party who is not represented by an attorney shall sign all papers and state the party's address and telephone number. The signature of an attorney or a party constitutes a certificate that the attorney or party has read the document; that to the best of the attorney's or party's knowledge, information, and belief formed after reasonable inquiry it is well grounded in fact and is warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law; and that it is not interposed for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation or administration of the case. If a document is not signed, it shall be stricken unless it is signed promptly after the omission is called to the attention of the person whose signature is required. If a document is signed in violation of this rule, the court on motion or on its own initiative, shall impose on the person who signed it, the represented party, or both, an appropriate sanction, which may be include an order to pay to the other party or parties the amount of the reasonable expenses incurred because of the filing of the document, including a reasonable attorney's fee.
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> (b) Verification. Except as otherwise specifically provided by these rules, papers filed in a case under the Code need not be verified. Whenever verification is required by these rules, an unsworn declaration as provided in 28 U.S.C. § 1746 satisfies the requirement of certification.

impose an appropriate sanction on the Debtor and his attorney (the "Debtor's Attorney") for their participation in: (1) a bad faith Chapter 11 filing; and (2) the Debtor's failure to schedule or otherwise disclose the various assets and financial transactions to the Bankruptcy Court that resulted in the Decision which revoked and denied the Debtor's discharge. The Sanction Motion further requested that the Court award Conklin $60,000.00 as an appropriate sanction.[3]

> (c) Copies of Signed or Verified Papers. When these rules require copies of a signed or verified paper, it shall suffice if the original is signed or verified and the copies are conformed to the original.

[3] Exhibit F to the Sanction Motion contained a summary of the time records of Conklin's attorney. This summary showed that in connection with the Debtor's bankruptcy case Conklin had incurred attorneys fees in the amount of $42,994.00, together with expenses of $6,436.84, and that $2,934.91 of those expenses had been included in an award of costs entered in the Conklin Discharge Proceeding. The summary also showed that over $25,000.00 of those

The Debtor's Attorney opposed the Sanction Motion. The Debtor did not even respond.

At a March 18, 1998 hearing, after it heard oral argument and reviewed the additional submissions of Conklin and the Debtor's Attorney, the Court indicated that it would issue a written Decision & Order which would: (1) deny the Sanction Motion as to the Debtor's Attorney because the Court had found that: (a) at the time of the filing of the Chapter 11 petition the Debtor's Attorney reasonably believed that the Debtor required relief under the Bankruptcy Code, and, given the extent of the Debtor's prior business, there was a possibility of proposing and funding a Chapter 11 reorganization plan; (b) the Debtor's Attorney had not signed either the Debtor's schedules or the monthly Chapter 11 debtor-in-possession financial reports which failed to disclose material assets and business transactions; (c) at the time they occurred, the Debtor's Attorney did not know of or participate in the Debtor's concealment of assets and financial records, failures to report assets or false oaths or accounts; and (d) the Debtor's Attorney did not represent the Debtor at the trial of the Conklin and Edgar Discharge Proceedings; (2) deny the Sanction Motion as to the Debtor to the extent that it was alleged that there had been a bad faith Chapter 11 filing; and (3) grant the Sanction Motion and impose an appropriate sanction against the Debtor for signing and filing his fraudulent schedules and monthly Chapter 11 debtor-in-possession financial reports on which he failed to disclose material assets and business transactions.

DISCUSSION AND CONCLUSION

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attorneys fees had been incurred in connection with the prosecution of the Conklin Discharge Proceeding.

From the Decision of Bankruptcy Judge Dorothy Eisenberg in *In re Dubrowsky*, 206 B.R. 30 (Bankr. E.D.N.Y. 1997) and the cases cited therein, we know that: (1) under Rule 9011 Bankruptcy Courts are required, or at a minimum have the discretion when the facts and circumstances of a case warrant it, to impose an appropriate sanction against a debtor for signing and filing schedules or other pleadings in a bankruptcy case that are knowingly and fraudulently false and which have resulted in the Debtor's discharge being denied or revoked pursuant to Section 727; (2) the appropriate sanction to be imposed under Rule 9011 in such circumstances is within the discretion of the Bankruptcy Court; and (3) an appropriate sanction should not be one that is more severe than reasonably necessary to deter repetition of the conduct by the offending person or comparable conduct by similarly situated persons.

As stated in the Decision: (1) the evidence presented in the trials of the Conklin and Edgar Discharge Proceedings clearly demonstrated that the Debtor knowingly, fraudulently and intentionally failed to disclose, in his schedules and his monthly Chapter 11 debtor-in-possession financial reports assets, financial transactions and financial interests which existed at the time of the filing of his petition or which were acquired post-petition while the Debtor was a debtor-in-possession under Chapter 11; (2) the Debtor was a sophisticated businessman and had engaged, prior to the filing of his petition, during the pendency of his Chapter 11 case, and subsequent to the conversion of his case to a Chapter 7 case, in a consistent pattern of putting assets in which he had a legal or an equitable interest beyond the knowledge and reach of his creditors and the Bankruptcy System; and (3) the Debtor's explanations at trial for his lack of disclosure regarding any legal or

equitable interests he may have had in a number of assets and business opportunities were completely unsatisfactory and not credible.

Based upon all of the facts and circumstances of the Debtor's bankruptcy case, I believe that it is a necessary and appropriate exercise of this Court's discretion to impose a sanction upon the Debtor under Rule 9011 and Section 105 of the Bankruptcy Code. I believe that an appropriate sanction is $12,500.00, which is to be paid within sixty (60) days to Conklin, as authorized by Rule 9011, to compensate him in part for the attorneys fees that he incurred in the prosecution of the Conklin Discharge Proceeding in which the Debtor had no meritorious defense regarding his fraudulent failure to disclose material assets and financial transactions. I believe that this sanction will give a clear message to the Debtor, and other potential debtors who are inclined to play "fast and loose" with disclosing their assets and financial affairs, that such an abuse will not be tolerated by this Court.

IT IS SO ORDERED.

/s/
HON. JOHN C. NINFO, II
U.S. BANKRUPTCY JUDGE

Dated: June 9, 1998